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STATE OF WASHINGTON

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STATE OF WASHINGTON

SUPREME COURT OF THE STATE OF WASHINGTON

WASHINGTON IMAGING SERVICES, LLC,

Respondent,

v.

WASHINGTON STATE DEPARTMENT OF REVENUE,

Petitioner.

PETITION FOR REVIEW

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ORIGINAL

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I. INTRODUCTION

This case concerns the application of business and occupation tax to a taxpayer that provided services to its customers in part by means of services it obtained through third parties. The Court should accept review because the Court of Appeals decision conflicts with this Court's decisions interpreting the definition of "gross income of the business" in RCW 82.04.080 and the Department of Revenue's rule, WAC 458-20-111.

The key question is whether funds paid by a client to a taxpayer may be excluded from the taxpayer's taxable "gross income," to the extent the taxpayer uses them to pay the third party, or are excludable as merely being "passed through" from the client to the third party. In prior cases where this Court addressed these issues, the tax liability of the parties turned on who contracted with whom and for what. The Court of Appeals failed to understand some key principles underlying the holdings in the cases and the B&O tax scheme generally. The resulting decision is contrary to existing caselaw.

There is a second reason this Court should accept review. Under the Court of Appeals's reasoning, any taxpayer that provides services using subcontractors or contracted labor can now argue that the portion of its receipts it pays to its subcontractors is excluded from the measure of its B&O tax if payment under the subcontract is contingent upon payment

being received under the primary contract. In other words, the Court of Appeals decision has the effect of creating a significant tax deduction that does not appear in the B&O tax statutes. Thus, the issue presented also is one of substantial public interest.

II. IDENTITY OF PETITIONER

The petitioner is the State of Washington, Department of Revenue, respondent in the Court of Appeals.

III. DECISION TO BE REVIEWED

The Department seeks review of the Court of Appeals, Division Two, decision in *Washington Imaging Services, LLC v. Washington State Department of Revenue*, Cause No. 38247-4-II, issued on September 22, 2009. *See* Appendix.¹

IV. ISSUE PRESENTED FOR REVIEW

In RCW 82.04.080, the Legislature broadly defined as taxable “gross income of the business” virtually all money a taxpayer receives “by reason of the transaction of the business engaged in . . . ,” without any deduction for labor or materials costs or any other expenses. The Department’s rule interpreting this definition, Rule 111, excludes from taxable “gross income of the business” certain amounts taxpayers receive

¹ The Appendix also includes the Court of Appeals order denying the Department’s timely motion for reconsideration and the order granting a nonparty’s motion to publish the decision, issued on December 15, 2009. This petition for review is timely filed under RAP 13.4(a).

from clients and pay, as agents on their clients' behalf, to third parties. Under RCW 82.04.080 and Rule 111, was the entire amount Washington Imaging Services ("WIS") received from patients or their insurers taxable gross income, where WIS paid a portion of that amount to an independent contractor for radiologists to interpret the medical images, but where the patients and insurers had no obligation to pay anyone but WIS?

V. STATEMENT OF THE CASE

During the relevant tax period, WIS was in the business of providing medical imaging services to patients. In advertising to the public WIS presented itself as "dedicated to providing state-of-the-art outpatient medical imaging services utilizing the most sophisticated imaging equipment." CP 135. Its product is a written interpretation of the images it produces "through its imaging technologies in the context of the patient's history by a qualified physician, in this case a fellowship trained radiologist, licensed to practice medicine in the State of Washington." CP 135; *see also* CP 91-92 (CEO's deposition testimony). WIS describes medical imaging services as involving two components, technical and professional. The "technical component" is generation of the medical image of the patient, such as an x-ray. The "professional component" is the radiologist's interpretation of the image. CP 33, 60, 101-02; App. Br.

at 10. Thus, WIS's product – what it sold to the public – included a radiologist's interpretation of the images created at WIS facilities.

WIS retained a professional corporation as an independent contractor to provide radiological interpretation of the images, Overlake Imaging Associates, P.C. ("Overlake"). CP 114. WIS and Overlake set forth their respective responsibilities and obligations in two documents, a "Medical Imaging Agreement" and an "Agency Agreement." CP 37-59; CP 60-62. WIS was responsible for billing patients and insurers. CP 50; CP 61.

WIS did not inform patients receiving medical imaging services of Overlake's existence or indicate that patients would have any obligation to pay Overlake as a result of the patient receiving medical imaging services through WIS. CP 112-13. Patients signed a patient registration form, in which they agreed to be financially responsible to WIS. CP 141. The patient registration form assigned insurance payments to WIS, not to anyone else. *Id.* The patient registration form made no mention of Overlake or of any agreement to pay Overlake. *Id.* Similarly, insurance companies contracted with WIS, but not with Overlake, to reimburse WIS for medical imaging services provided at WIS locations. CP 99-100.

WIS billed patients or insurance companies for both the technical component (producing the image) and the professional component (the

radiologist's interpretation of the image) of the medical imaging services. CP 95. The bill did not set forth a separate charge for each component, but billed the two components together in one "global" charge for medical imaging services. *Id.*; CP 103-04, 143. The bill was on WIS letterhead, asked that payment be remitted to WIS, and made no reference to Overlake whatsoever. CP 143. The bill did not indicate that WIS was acting as a billing agent for Overlake, that patients or insurance companies owed a fee to Overlake, or that WIS would act as an agent for patients or insurance companies to pay Overlake. *Id.*

Consistent with the way WIS generated its bills, when WIS received payment, the payment was a lump sum and not separated into components. CP 98. Patients had no say in how much of the payment on the "global bill" was transmitted to Overlake. CP 98-99. Insurance companies making payments to WIS similarly had no say in how much of the global payment was paid to Overlake. CP 99. Rather, the percentage of the payment on the "global bill" paid to Overlake depended entirely on the negotiated contract between WIS and Overlake. CP 121.

In their contract, WIS and Overlake determined the percentage of net collections that would be paid to Overlake. CP 50, 104. Originally, these percentages were based on Medicare reimbursement rates for each procedure, which separated the components. CP 104. But rather than use

the percentage Medicare reimbursement rates indicated on any given procedure, WIS and Overlake averaged numerous procedures into several broad categories of imaging, and through negotiation determined how they would split the global fee in each category. CP 50, 104.

Once these percentages were agreed to, the contract obligated WIS to pay the percentages even though the Medicare reimbursement rates changed over time. CP 107-08, 122-23. Thus, WIS's obligation to Overlake depended entirely on the terms negotiated in its contract with Overlake rather than any Medicare reimbursement rates or direction from patients or insurance companies.

The Department audited WIS for the period January 2000 through June 2005, and issued two assessments. CP 5. The Department's Appeals Division affirmed the assessments, and WIS paid them in full. CP 6. In September 2007, WIS filed a refund action in Thurston County Superior Court under RCW 82.32.180. CP 4-8. The Honorable Gary R. Tabor granted summary judgment to the Department. CP 175-76.

On review, the Court of Appeals held in an unpublished decision that the amounts WIS paid to Overlake were payments WIS collected "much like a collection agency for services Overlake renders and, as such, are not gross income to WIS' business." *Washington Imaging*, Slip Op. at 1. It reversed the trial court's order and remanded for entry of summary

judgment in favor of WIS. *Id.* at 1, 14. The Department filed a motion for reconsideration, which the Court of Appeals denied on December 2, 2009. A nonparty law firm with clients in the health care industry filed a motion to publish, which the Department opposed, but which the Court of Appeals granted on December 15, 2009. *See* orders in Appendix.

VI. ARGUMENT IN SUPPORT OF REVIEW

This Court should accept review under RAP 13.4(b)(1), (b)(2) or (b)(4). The Court of Appeals decision in this case is in conflict with at least three prior decisions of this Court addressing the same tax issue, *i.e.*, whether monies received by a taxpayer were taxable as gross income to the taxpayer or excludable as amounts merely “passed through” to third parties. The decision also is in conflict with prior Court of Appeals decisions. Review also is appropriate because the Court of Appeals decision, if left standing, substantially narrows what constitutes taxable “gross income of the business,” effectively creating a deduction for payments to subcontractors that has not been authorized by the Legislature. This is an issue of substantial public interest that should be addressed by this Court.

A. The Court Of Appeals Decision Conflicts With Supreme Court Decisions: Amounts WIS Paid To Overlake Were A Cost Of Doing Business Because WIS Was The Sole Party With Any Liability To Pay Overlake.

The B&O tax is imposed on every person “for the act or privilege of engaging in business activities” and applies to the “gross income of the business.” RCW 82.04.220. The Legislature “intended to impose the business and occupation tax upon virtually all business activities carried on within the state.” *Simpson Inv. Co. v. Dep’t of Revenue*, 141 Wn.2d 139, 149, 3 P.3d 741 (2000) (quoting *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971)). As a result, unless an exemption or deduction applies, a taxpayer owes B&O tax on all income received for the rendition of services, including services related to health care.

Under RCW 82.04.080, “gross income of the business” means:

[T]he value proceeding or accruing *by reason of the transaction of the business engaged in* and includes gross proceeds of sales, compensation for the rendition of services, . . . all without any deduction on account of . . . labor costs, . . . or any other expense whatsoever paid or accrued

(Emphasis added). The business in which WIS is engaged is providing medical imaging services to the public. CP 101-02; CP 135.

In Rule 111, the Department has interpreted the definition of “gross income” to allow a business to exclude from reported gross income “advances” or “reimbursements” that merely “pass through” the business

when it receives payments as an agent. *See* Appendix D. An exclusion from taxable income is allowed because “pass-through” amounts are not income attributable to the business activities of the agent. *City of Tacoma v. Wm. Rogers Co.*, 148 Wn.2d 169, 175, 60 P.3d 79 (2003). Under Rule 111, which has remained unchanged since 1947, the exclusion applies only when “the customer or client alone is liable for the payment of the fees or costs, and when the taxpayer making the payment has no personal liability therefor, either primarily or secondarily, other than as agent for the customer or client.” The Court of Appeals acknowledged that Rule 111 sets the bar for tax exclusions relatively high, requiring taxpayers to meet several conditions. Slip Op. at 4 (citing *Christensen, O’Connor, Garrison & Havelka v. Dep’t of Revenue*, 97 Wn.2d 764, 768, 649 P.2d 839 (1982)).

1. **A client must be liable to a third-party service provider before a taxpayer may claim funds it receives from the client are merely “passed through” to the third party.**

Both this Court and the Court of Appeals have interpreted and applied the definition of “gross income of the business” and Rule 111 in circumstances where taxpayers have claimed an exclusion from tax for amounts they received and then paid to third parties. *See Wm. Rogers*, 148 Wn.2d 175-81 (wages paid by temporary staffing service to its workers were not excludable as “pass-through” payments; interpreting identical

city tax); *Rho Co. v. Dep't of Revenue*, 113 Wn.2d 561, 573, 782 P.2d 986 (1989) (remanding for determination whether temporary employment service acted solely as the agent of its clients in paying temporary workers); *Walthew, Warner, Keefe, Arron, Costello & Thompson v. Dep't of Revenue*, 103 Wn.2d 183, 187-88, 691 P.2d 559 (1984) (law firm not taxable for litigation expenses paid to third-party providers where clients were ultimately liable for paying third-parties; discussing relationship between Rule 111 and B&O tax statutes); *Christensen*, 97 Wn.2d at 768-72 (where law firm did not assume liability for paying third parties for patent search and patent application services, amounts forwarded by law firm could be excluded from its gross income); *Pilcher v. Dep't of Revenue*, 112 Wn. App. 428, 435-42, 49 P.3d 947 (2002) (physician agreeing to staff and operate a hospital emergency room was taxable on amounts he received and then paid to subcontractor physicians where he was solely responsible for paying the physicians he retained), *rev. denied*, 149 Wn.2d 1004 (2003); *Medical Consultants Northwest, Inc. v. State*, 89 Wn. App. 39, 44-48, 947 P.2d 784 (1997) (medical consulting firm could exclude amounts paid to physicians serving as consultants for independent medical examinations where trial court found only the client/patient had liability for paying the physician), *rev. denied*, 136 Wn.2d 1002 (1998).

In the foregoing cases, the courts determined the taxpayer's tax liability for money it received based in significant part on who, between the taxpayer and its client, had the legal obligation to pay the third party. Whether funds qualify as taxable "gross income" or excludable "pass-through" amounts under Rule 111 depends on the answer to that question.

For instance, in *Walthew*, this Court's holding that funds a law firm received were not taxable turned on the fact that the clients, not the law firm, were liable for paying the third parties. *Walthew*, 103 Wn.2d at 186-90. As a factual matter, the clients assumed the obligation when they signed contracts with the law firm confirming they would pay those third-party costs. *Id.* at 185. And as a legal matter, the attorney ethics rules required clients to retain ultimate liability for those expenses. *Id.* at 185, 188-89. Thus, when the law firm received funds from clients as an advance or reimbursement of those expenses, the law firm was acting "solely as agent for the client." *Id.* at 188.

Contrary to the Court of Appeals decision, Slip Op. at 10-11, this Court in *Walthew* did not reject a "complete package/cost of doing business" argument for all cases, regardless of the facts. It rejected the argument in that case where the facts and the law established that the law firm was acting solely as an agent for clients when it paid third parties for

certain litigation expenses, and the clients remained “ultimately liable” for those payments. *Id.* at 185, 187-89.

In its most recent case addressing “gross income” and Rule 111, this Court continued to focus on determining whether the taxpayer or the client were liable for the payments:

If a taxpayer assumes any liability beyond that of an agent, the payments it receives are not “pass through” payments, even if the taxpayer uses the payments to pay costs related to the services it provided to its client.

City of Tacoma v. Wm. Rogers Co., 148 Wn.2d 169, 178, 60 P.3d 79 (2003) (citing *Walthew*, 103 Wn.2d at 189). This Court emphasized that in *Walthew* and the other law firm case, *Christensen*, “the taxpayer clearly had no liability for the payments.” *Wm. Rogers*, 148 Wn.2d at 177. In contrast, in *Wm. Rogers*, the temporary staffing company had “sole liability to pay the workers.” *Id.* at 179.²

In this case, the Court of Appeals concluded, relying on *Medical Consultants*, that because WIS only had an obligation to pay Overlake for

² In *Rho*, the other temporary staffing case, this Court noted the absence of a stipulation by the parties establishing whether the client or the staffing service had ultimate liability for paying the temporary employees. *Rho*, 113 Wn.2d at 569. The Court turned to the rules of agency for guidance and remanded the case for further proceedings on whether the taxpayer was acting solely as an agent for its clients. *Id.* at 569-73. The two dissenting Justices would have affirmed the tax assessment, based in large part on *Rho*’s liability for paying the employees under its contracts with them and with its clients. “The basic tool [Rule 111] uses to make this distinction between costs of doing business and pass-through costs is liability on the part of the taxpayer. If the taxpayer is liable for the amounts in question, they are costs of doing business.” *Id.* at 582 (Dore, J., dissenting).

radiology services if WIS first received payment from patients or their insurers, WIS had no primary or secondary liability to Overlake and merely collected and passed through payments to Overlake. Slip Op. at 7-10. However, *Medical Consultants* is inapposite because in that case, just as in *Walthew*, the client, not the taxpayer, was ultimately liable for paying the third party.

In *Medical Consultants*, the parties submitted stipulated facts on which the trial court relied to make a finding of fact that “only the client has liability for paying the physician.” *Medical Consultants*, 89 Wn. App. at 44. On appeal, the Court of Appeals held the trial court’s finding was a permissible inference to draw from the evidence. *Id.* at 45. The Court buttressed its holding that the finding of fact was permissible with the trial court’s explanation that Medical Consultants had no obligation to pay a third-party physician if it was unable to collect the fee from the client. *Id.*³

The Court of Appeals in this case seems to have read *Medical Consultants* as holding that when a payment obligation from Party B to Party C is contingent upon Party B receiving payment from Party A, Party A necessarily has liability to pay Party C. This is clearly incorrect, both logically and legally. See, e.g., *Impecoven v. Dep’t of Revenue*, 120

³ Other evidence in the record also supported this finding of fact. *Medical Consultants*, 89 Wn. App. at 43 (describing payment details, including that clients were responsible to physicians for no-show fee and paying physicians for any testimony).

Wn.2d 357, 841 P.2d 752 (1992) (entire commission paid by insurance company to insurance agent is gross income despite percentage paid to sub-agent; sub-agent not paid unless agent paid, but had no right to receive money directly from insurance company). The holding in *Medical Consultants* should be limited to its facts and its procedural posture.

Here, the billing procedure was similar to that in *Medical Consultants* because WIS was not liable to pay Overlake if it did not receive payments from the patients/insurers. CP 50; Slip Op. at 3, 12. What is missing, however, is any finding or even any evidence that the patients or insurers were themselves liable to pay Overlake for the radiology services Overlake performed under contract to WIS.

The Court of Appeals decision does not address whether the patients or insurers had any obligation to pay Overlake. Thus, it implies that funds paid to a taxpayer by a client may be excluded from the taxpayer's "gross income" and may be considered "pass-through" payments to a third party, *even if the client has no legal obligation or liability to pay the third party*. In this respect, the Court of Appeals decision in this case conflicts with *Walthew*, *Wm. Rogers*, and *Christensen*, which provides a basis for review under RAP 13.4(b)(1). For the same reasons, the decision also is in conflict with *Pilcher* and even

Medical Consultants, which provides a basis for review under RAP 13.4(b)(2).

2. A taxpayer's conditional liability is not the equivalent of no liability.

In addition to being in conflict with appellate cases applying Rule 111, the Court of Appeals decision could create confusion in other contexts. The Court of Appeals repeated an error in *Medical Consultants*, which was to equate a taxpayer's *conditional* liability (contractual disclaimer of liability under certain circumstances) with the *absence* of liability (*i.e.*, where the clients are ultimately or solely liable) for purposes of pass-through treatment. However, that analysis is inconsistent with commercial law.

In contracts, "primary" liability means unconditional liability, and "secondary" liability means there is a condition precedent to the promisor's duty to perform. *Warren v. Washington Trust Bank*, 19 Wn. App. 348, 355-56, 575 P.2d 1077 (1978), *affirmed as modified*, 92 Wn.2d 381, 598 P.2d 701 (1979). Under its agreement with Overlake, WIS thus has secondary contractual liability to pay Overlake. But the decision appears to hold as a matter of law that WIS's secondary contractual liability is the equivalent of having no liability at all. The Court's

incorrect assumption about forms of contract liability also supports review by this Court.

3. The Court of Appeals confused the role of collection agencies with that of WIS, a medical imaging business.

In their contracts with each other, WIS and Overlake designated WIS as Overlake's "collection agent" for purposes of Overlake's share of the fees WIS received from patients or insurers. CP 49-50; 60-62. The Court of Appeals treated this contract term as controlling the tax issue and concluded that WIS functioned merely as a collection agency with respect to funds paid to Overlake. Slip Op. at 1, 13. The Court erroneously reached this conclusion because it did not consider whether WIS's patients had any liability to pay Overlake. A collection agent does not collect from debtors for services it has provided or for money the debtors owe to it. A debtor paying a collection agent for a dentist would not think the collection agency had provided dental services. A collection agency is paid by its client to collect money a third party owes to the client. Thus, as the Department acknowledged at oral argument in the Court of Appeals, the money a collection agency collects on behalf of a creditor is not the collection agency's gross income because the debtor owes the money to the creditor, not the collection agency.

Here, WIS admits it is engaged in the business of providing medical imaging services, which includes the professional interpretation of those images. CP 91-92, 135. WIS's business is therefore not like a collection agency.⁴ Money WIS received for providing medical imaging services was therefore the "value proceeding or accruing by reason of the transaction of the business [WIS] engaged in" and constituted gross income of WIS.⁵ See RCW 82.04.080. Likewise, because neither patients nor insurers had any obligation to pay anyone other than WIS, including Overlake, under the undisputed evidence WIS could not have been acting merely as Overlake's collection agent.

The Court of Appeals decision is in conflict with *Wm. Rogers*, *Walthev*, *Christensen*, and *Pilcher* because it fails to apply the standards enunciated in those cases for applying RCW 82.04.080 and Rule 111. In particular, it allows tax-exempt status for money WIS received for providing medical imaging services, when WIS was the only party liable to pay Overlake for radiology interpretations.

⁴ Nor can WIS change the taxability of this revenue by terms in its agreement with Overlake. Cf. *City of Seattle v. Ford Motor Co.* 160 Wn.2d 32, 43-44, 156 P.3d 185 (2007) (terms in contract do not control whether sale is taxable in Washington), *cert. denied*, 128 S. Ct. 1224 (2008); see also Brief of Respondent at 15-21. In other words, what WIS did with the money after receiving it cannot change the fact that the money is consideration for services WIS sold to the public.

⁵ The Court's reliance on the fact that WIS did not itself physically provide the services but did so through an independent contractor overlooks *Pilcher v. Dep't of Revenue*, 112 Wn. App. 428, 440, 49 P.3d 947 (2002), which held this is immaterial.

B. The Court Of Appeals Decision Creates An Issue Of Substantial Public Interest By Effectively Treating The B&O Tax As A Net Income Tax Instead Of A Gross Receipts Tax.

This Court has emphasized that the B&O tax “is not a tax on either profit or net gain . . . , but a tax on the total money or money’s worth received in the course of doing business.” *Budget Rent-A-Car of Wash.-Ore., Inc. v. Dep’t of Revenue*, 81 Wn.2d 171, 173, 500 P.2d 764 (1972). It is a gross receipts tax, not a net income tax. *See, e.g., Tyler Pipe Indus., Inc. v. Dep’t of Revenue*, 105 Wn.2d 318, 327, 715 P.2d 123 (1986). In the absence of a statutory deduction or exemption, taxpayers may not deduct their costs of doing business.

The Court of Appeals seemed uncomfortable with the notion that both WIS and Overlake might owe B&O tax on money paid by patients for medical imaging services – WIS on the total fee, and Overlake on the portion WIS paid it under their contract. Slip Op. at 5 & n.2. But this Court has on several occasions recognized that the B&O tax has a pyramiding effect. The gross receipts of several taxpayers may ultimately result from the same source, “but each activity is separate and each may be taxed.” *Impecoven*, 120 Wn.2d at 364 (citing *Supply Laundry Co. v. Jenner*, 178 Wash. 72, 79, 34 P.2d 363 (1934)); *First Am. Title Ins. Co. v.*

Dep't of Revenue, 144 Wn.2d 300, 305, 27 P.3d 604 (2001) (citing *Impecoven*, 120 Wn.2d at 363-64).⁶

The Court of Appeals decision improperly allows taxpayers that subcontract out part of the services they sell to their customers to exclude from taxation what should be a nondeductible cost of doing business. Effectively, the decision allows the gross income tax to be applied as a net income tax in these circumstances. Applied consistently, this holding would radically change taxation in the construction industry alone, where amounts paid to subcontractors hired by a general contractor are treated as the contractor's cost of doing business. *See* WAC 458-20-170. In other industries, employers would have an incentive to convert employees into independent contractors. In this manner, they could avoid paying B&O taxes on amounts received from clients that previously were paid to employees, but now would be paid to contract workers. All taxpayers would need to do to avoid paying tax on amounts they pay to their

⁶ The pyramiding nature of gross receipts taxes, including Washington's B&O tax, makes them a target of criticism by tax policy commentators and the business community. *See, e.g.,* Tax Foundation, *Special Report – Tax Pyramiding: The Economic Consequences of Gross Receipts Taxes* (No. 147, Dec. 2006). The policy decision whether to have a gross receipts tax belongs, of course, to the Legislature. The Legislature enacted the B&O tax in 1935 after this Court held that the net income tax it previously enacted violated the Fourteenth Amendment of the Washington Constitution. *See Culliton v. Chase*, 174 Wash. 363, 25 P.2d 81 (1933).

subcontractors is to condition payment to the subcontractors on receiving payment from their clients.⁷

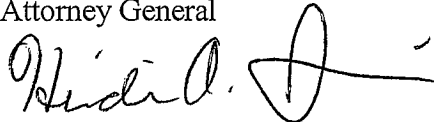
Regardless of what the Court of Appeals understood about the B&O tax, the Court issued a decision that will generate further litigation by taxpayers in multiple industries. Taxpayers will claim a tax exclusion based on the decision in this case even though they cannot meet the requirements in Rule 111 and this Court's cases applying it. The Department will continue to rely on *Wm. Rogers*, *Walthew*, *Pilcher*, and other Rule 111 cases. Accordingly, there will be no resolution of the confusion the Court of Appeals decision creates until this Court weighs in on the significance of a taxpayer's conditional liability clause in a contract with a third party.

VII. CONCLUSION

For the foregoing reasons, the Department requests that this Court grant this petition for review.

RESPECTFULLY SUBMITTED this 14th day of January, 2010.

ROBERT M. MCKENNA
Attorney General



HEIDI A. IRVIN, WSBA No. 17500
PETER B. GONICK, WSBA No. 25616

⁷ City B&O taxes will be similarly affected by the Court of Appeals decision.

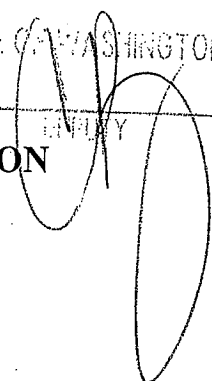
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ATTORNEY GENERALS OFFICE
REVENUE DIVISION

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DIVISION II

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STATE OF WASHINGTON

BY 

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

DIVISION II

WASHINGTON IMAGING SERVICES,
LLC,

No. 38247-4-II

Appellant,

v.

WASHINGTON STATE DEPARTMENT OF
REVENUE,

UNPUBLISHED OPINION

Respondent.

QUINN-BRINTNALL, J. — Washington Imaging Services, LLC (WIS) appeals the trial court's grant of summary judgment in favor of the State Department of Revenue (DOR). The trial court found the funds that WIS collects from its patients or its patients' insurance companies and forwards to Overlake Imaging Associates, P.C., are gross income to WIS and subject to Washington's business and occupation (B&O) tax. We hold that these funds are payments WIS collects much like a collection agency for services that Overlake renders and, as such, are not gross income to WIS' business and are not subject to Washington's B&O tax. Accordingly, we reverse and remand.

FACTS

WIS

WIS is a Washington limited liability company that operates medical imaging facilities in Bellevue and Issaquah, Washington. At these facilities, WIS provides all of the equipment and supplies necessary to produce medical images, including magnetic resonance imaging (MRI) scans, computed tomography (CT) scans, positron emission tomography (PET) scans, x-rays,

APPENDIX A

and other forms or modalities of medical images. WIS employs administrative support staff as well as trained technicians who operate and maintain the medical imaging equipment.

WIS provides medical imaging services for patients referred by their treating physicians. WIS ultimately provides these treating physicians with a written report that contains medical image information to assist in the diagnosis and treatment of their patients. WIS generates the medical image and, because it does not have a medical license, contracts for the professional medical interpretation of the image by a radiologist. WIS contracts with Overlake, a group of radiologists, for the professional medical interpretation of WIS' images.

WIS and Overlake have two contracts. The first contract, signed in 1996, governs the terms and conditions under which Overlake provides the professional medical services of its radiologists to provide medical interpretations of WIS' images. Under the second contract, WIS submits a single global bill directly to the patients' insurance companies for both its fee, which it refers to as "technical charges," and Overlake's interpretation fee, which it refers to as "professional charges"; such a single global bill is customary in the outpatient medical imaging business.¹

Overlake and WIS entered into a second contract only after Overlake's previous third party billing company ceased service in 2001. Under the second contract, WIS collects both its

¹ Insurance companies also prefer global billing because it is far more efficient and, therefore, less expensive for the health insurance companies to deal with a single bill that contains all charges for a health care service than to deal with two partial bills for a patient's health care services. In fact, the record shows that the insurance companies will not pay a patient's isolated bill for either the technical fee or the professional fee. Before an insurance company will pay either fee, it must have been billed for both the technical and professional fees and it must have been able to match both bills to a single procedure.

fee and Overlake's fee and passes on to Overlake the professional fee less an agreed upon service charge calculated as a percentage of the professional fee amount WIS collected. Of importance here, this second contract provides that WIS has no ownership interest in that portion of payment allocated for Overlake's professional fees; rather, WIS acts as the collection agent for Overlake's fees. In this second contract, Overlake also agreed that WIS could bill for its fees and Overlake's fees in one "global bill" as insurance companies require. The patients' insurance company then issues its payments for both the professional and technical services in a single global payment, without designating what portion of the payment is for each type of service. If the global bill that WIS issues to the patients' insurance company, or the patients, is not paid, WIS does not have any obligation to pay Overlake for Overlake's professional services.

If the insurance does not cover the entire amount of the bill, WIS sends the patients a secondary bill for the amount of the patients' responsibility. The secondary bill to the patients identifies the radiologist who interpreted the image, the initial charge for all services, any adjustment of that charge made by the insurance company, the amount paid by the insurance company, and the remaining amount the patients owe under his or her policy.

B&O TAX

Washington taxes the right to do business in this state by imposing a B&O tax on the "gross income" of a business. RCW 82.04.220. The legislature intended to impose the B&O tax on virtually all business activities in the state. *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 149, 3 P.3d 741 (2000) (quoting *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971)). Taxation is generally the rule and deductions or exemptions are the exception. *Columbia Irrigation Dist. v. Benton County*, 149 Wash. 234, 240, 270 P. 813 (1928). Tax exemptions and deductions must be narrowly construed. *Crown Zellerbach Corp. v. State*, 45

Wn.2d 749, 757-58, 278 P.2d 305 (1954). Washington's B&O tax does apply to health care services. See RCW 82.04.322, .4297, .431 (allowing for B&O tax exemptions and deductions for various aspects of health services).

DOR has created an exemption when a business receives and handles money for reasons other than as compensation for goods or services it sold. WAC 458-20-111 ("Rule 111"). Under Rule 111, a business can exclude from its taxable gross income amounts it receives solely as an agent for a client, which the business (as agent) must pay on the client's behalf to third parties. WAC 458-20-111. DOR cites a car dealership's collection of sales tax as a classic example of this type of payment. WAC 458-20-111. Because the sales tax is collected from the purchaser and passed immediately to the state, these payments are frequently described as "pass-through" payments.

Although the "pass-through" concept appears to be relatively simple, DOR and taxpayers often disagree about the circumstances under which it applies. Rule 111 sets the bar for tax exclusions relatively high, requiring taxpayers to meet several conditions. *Christensen, O'Connor, Garrison & Havelka v. Dep't of Revenue*, 97 Wn.2d 764, 768, 649 P.2d 839 (1982). If any one of the conditions is missing, then the taxpayer's receipts are deemed taxable gross income of the business under RCW 82.04.080 and the B&O tax is due. See *Christensen*, 97 Wn.2d at 768. Likewise, if a taxpayer's receipts are in fact gross income of the business, the taxpayer cannot prove Rule 111 requirements to exclude them from being taxed.

DOR AUDIT OF WIS

In late 2005, DOR audited WIS for the period January 2000 through June 2005. DOR concluded that WIS underpaid its B&O tax for the audit period because it had not included in its gross income the money it collected and subsequently forwarded to Overlake as compensation

for the professional medical interpretation services Overlake provided. WIS unsuccessfully contested the audit and, on August 21, 2007, WIS paid \$250,597.79 under protest, with interest and penalties, and promptly sued DOR for a refund. WIS and DOR agreed that no genuine issues of material fact existed and both parties moved for summary judgment. On August 15, 2008, the trial court denied WIS' motion for summary judgment and granted summary judgment in favor of DOR.

The question we address in this appeal is whether the money that WIS, a medical imaging services business, receives from patients or the patients' insurance companies and pays to Overlake, a professional services corporation, is taxable as gross income to WIS, as well as Overlake.²

ANALYSIS

STANDARD OF REVIEW

We review an order on summary judgment de novo. *Hisle v. Todd Pac. Shipyards Corp.*, 151 Wn.2d 853, 860, 93 P.3d 108 (2004). Summary judgment is appropriate only if “the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.” CR 56(c). We view all facts in the light most favorable to the nonmoving party. *Vallandigham v. Clover Park Sch. Dist. No. 400*, 154 Wn.2d

² During oral argument, DOR asserted that because B&O tax is a pyramiding-type tax, not a value-added-type tax, both WIS and Overlake are required to pay B&O tax on these funds. Wash. State Court of Appeals oral argument, *Washington Imaging Services, LLC v. Dep't of Revenue*, No. 38247-4-II (May 8, 2009), at 23 min. 45 sec.

16, 26, 109 P.3d 805 (2005). Summary judgment is appropriate only if reasonable persons could reach but one conclusion from all the evidence. *Vallandigham*, 154 Wn.2d at 26.

Agency rules are subject to the same principles of interpretation as statutes. *See Seattle FilmWorks, Inc. v. Dep't of Revenue*, 106 Wn. App. 448, 453, 24 P.3d 460, review denied, 145 Wn.2d 1009 (2001). Generally, taxation is the rule and exemptions and deductions are the exception. *Columbia Irrigation Dist.*, 149 Wash. At 240. Because of the broad application of Washington's taxing statutes, we narrowly construe tax deductions and exemption statutes. *Crown Zellerbach Corp.*, 45 Wn.2d at 757-58; accord *United Parcel Serv., Inc. v. Dep't of Revenue*, 102 Wn.2d 355, 360, 687 P.2d 186 (1984); accord *Budget Rent-A-Car of Wash.-Or., Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 174-75, 500 P.2d 764 (1972). We construe any ambiguity in such a statute strictly, but fairly, against the taxpayer. *Group Health Coop. of Puget Sound, Inc. v. Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967); *Crown Zellerbach Corp.*, 45 Wn.2d at 757-58. The taxpayer bears the burden of proving that it qualifies for a tax deduction. *Group Health*, 72 Wn.2d at 429.

GROSS INCOME

Washington levies a B&O tax on a business's gross income, including compensation for "rendition of services." RCW 82.04.080. RCW 84.04.080 defines gross income of the business as

the value proceeding or accruing by reason of the *transaction of the business engaged in* and includes gross proceeds of sales, *compensation for the rendition of services*, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

(Emphasis added.)

Under this broad definition, a service provider may not deduct any of its own costs of doing business from its gross income. *Rho Co., Inc. v. Dep't of Revenue*, 113 Wn.2d 561, 566-67, 782 P.2d 986 (1989).

Here, WIS argues that the funds it collects and passes to Overlake are not gross income under RCW 82.04.080. DOR contends that unless WIS satisfies the requirements of Rule 111, the funds at issue are the cost of doing business and are included in gross income as a matter of law. For the reasons stated below, we agree with WIS.

Our decision in *Medical Consultants Northwest, Inc. v. State*, 89 Wn. App. 39, 947 P.2d 784 (1997), *review denied*, 136 Wn.2d 1002 (1998), informs our decision here. Citing *Medical Consultants*, WIS argues that the funds it receives from patients and subsequently pays to Overlake do not constitute gross income because the funds are not “compensation for services rendered by WIS.” Br. of Appellant at 17. DOR responds first that the facts in *Medical Consultants* are materially different from the facts here and, second, that these funds do constitute compensation for services WIS rendered because “WIS offers the public complete medical imaging services, bills for complete medical imaging services, and is paid for complete medical imaging services.” Br. of Resp’t at 13 (emphasis omitted). As a result, DOR argues that the funds are simply a cost of doing business for WIS. Again, we agree with WIS.

In *Medical Consultants*, the taxpayer, [Medical Consultants Northwest (MCN)], was in the business of providing objective medical opinions in the form of written reports; these written opinions were based on medical exams performed by independent physicians. 89 Wn. App. at 41. Because MCN did not have a license to practice medicine, it contracted with individual physicians to conduct independent medical examinations (IMEs) on behalf of MCN’s clients.

Med. Consultants, 89 Wn. App. at 42. MCN then completed a written report based on the physician's notes; after completing the report, MCN billed its clients for services it provided as well as the IMEs conducted by the independent physicians; the client paid the total fee for services in one check. *Med. Consultants*, 89 Wn. App. at 42. Upon receipt of the payment, MCN forwarded the allocable portion to the physician for services rendered. *Med. Consultants*, 89 Wn. App. at 42. Under these facts, we held that "[t]he monies MCN collects for medical exams are not for MCN's 'rendition of services,' but rather are passed through to the actual renderers of the medical examination services, i.e., the physicians." *Med. Consultants*, 89 Wn. App. at 48.

Here, the undisputed facts are virtually identical to those in *Medical Consultants*. Much like MCN, WIS is in the business of providing objective medical opinions in the form of a written report based on the Overlake radiologists' professional medical interpretation of the image WIS produces. Also, because WIS does not have a license to practice medicine, it contracts with Overlake to obtain the professional medical interpretation of the patients' imaging exam, over which the Overlake radiologists have complete control. WIS administrative staff convert the radiologist's interpretation of the image into a written report and submit that report to the radiologist for signature. Importantly, like in MCN, WIS submits to its patients' insurance companies a single global bill for the technical services it rendered as well as for the professional services Overlake rendered. The insurance company pays WIS in one check and WIS then forwards the allocable portion of the payment to Overlake for the professional medical services that Overlake's radiologist rendered. As in *Medical Consultants*, the money WIS collects for the professional medical interpretation of its medical images does not constitute payment for WIS' "rendition of services," but is "passed through" to the actual renderers of the professional

medical interpretation services, i.e., the Overlake radiologists. 89 Wn. App. at 48. Despite DOR's argument to the contrary, we see no meaningful distinction between the stipulated facts in *Medical Consultants* and the undisputed facts here.

DOR contends that the facts in *Medical Consultants* are "materially different" because MCN operated as a consulting business and worked to facilitate the examining physician's service as a medical consultant for the client. Br. of Resp't at 24. DOR also points out that if the client wished to have the consulting physician testify on his or her behalf, the client would need to arrange for this directly with the consulting physician. As a result, DOR argues that the "key relationship from a business perspective" in *Medical Consultants* was between the client and the consulting physician. Br. of Resp't at 22. But even assuming that DOR is correct about this "key business relationship," which we do not, such a distinction is not a difference that renders our opinion in *Medical Consultants* inapposite.

DOR also argues that the trial court's finding in *Medical Consultants*—that only MCN clients were liable for payment to the physicians—is a material distinction. But in *Medical Consultants*, DOR stipulated that MCN was not obligated to pay the physicians for their services if MCN was unable to collect the fee from its clients. 89 Wn. App. at 41-43. As a result, we held that (1) only the MCN client had liability for paying the physician; (2) if the client did not pay, MCN did not have primary or secondary liability for the payment; and (3) if the client did pay, MCN's liability was only to forward that payment to the physician. *Med. Consultants*, 89 Wn. App. at 44-45. Here, DOR "does not dispute that WIS paid Overlake a percentage of net amounts *actually* collected from patients" or that WIS was "not obligated . . . to pay Overlake for its professional fees *unless* WIS received payment from patients." Br. of Resp't at 40 (emphasis

added) (citing Clerk's Papers (CP) at 50). We see no material distinction between MCN's and WIS' billing procedures.

COMPLETE PACKAGE/COST OF DOING BUSINESS

Next, DOR contends that WIS provides an inseparable, complete package of services that includes Overlake's professional medical services and, as a result, the payments WIS makes to Overlake are simply part of WIS' "cost of doing business," which is included in the gross income of a business. Br. of Resp't at 15. Specifically, DOR contends that because WIS enters into an arrangement with patients in which WIS patients are provided "complete medical imaging services, WIS [is] compensated for the services it render[s], with the assistance of its independent contractor[,] Overlake," and WIS bills its patients "for the complete service and [is] paid for the complete service," the "total amount of funds it collect[s] constitute[s] 'gross income of the business.'" Br. of Resp't at 21.

We agree that business costs are not exempt from a B&O tax, but DOR made a virtually identical "complete package/cost of doing business" argument in *Walthew, Warner, Keefe, Arron, Costello & Thompson v. Dep't of Revenue*, 103 Wn.2d 183, 187, 691 P.2d 559 (1984), which our Supreme Court soundly rejected. In *Walthew*, our Supreme Court ultimately held that a law firm was not required to pay the state B&O tax on client reimbursements for payments the law firm made to court reporters, physicians, and process servers because (1) these advances remained the obligation of the client; and (2) the law firm, at most, assumed liability only as the client's agent. 103 Wn.2d at 190. DOR argued that Rule 111 excluded only incidental costs that were not necessary to the taxpayer's business; therefore, according to DOR's interpretation of its Rule 111, funds paid to a taxpayer that are passed through to a third party provider of services essential to the taxpayer's business represented the taxpayer's cost of doing business that may

not be excluded from the taxpayer's gross income. *Walthew*, 103 Wn.2d at 187. But the *Walthew* court rejected DOR's argument. Based on the language of RCW 82.04.080 and .090, the court reasoned that the funds at issue in *Walthew*, funds paid by the clients to the law firm, were not compensation for the rendition of services by the law firm but rather were passed through to pay for services essential to the processing of the litigation but rendered by third party providers. 103 Wn.2d at 187-89.

Here, like *Walthew*, DOR contends that all amounts paid to and through WIS constitute compensation for WIS' business of "complete medical imaging services . . . and is paid for complete medical imaging services" (Br. of Resp't at 19) regardless of whether WIS itself renders all services essential to this business or these essential services are rendered "through independent contractors or otherwise." CP at 72. Thus, just as DOR argued in *Walthew*, DOR argues here that the funds that WIS owes and pays to Overlake are a cost of doing business as a medical imaging service. DOR argues that the final product that WIS produces is a medical report that includes the Overlake radiologists' professional interpretation of the medical image WIS produced but this is precisely the same final product provided by MCN in *Medical Consultants*.

We hold that the reasons our Supreme Court rejected DOR's "complete package" argument in *Walthew* apply here. In *Walthew*, the funds that flowed to the law firm to pay the costs of third parties who provided services necessary for the operation of the law firm's business were not part of the law firm's gross income because the law firm (1) could not provide these services as a cost of doing business and (2) was not liable either primarily or secondarily for these third party services. 103 Wn.2d at 188-89.

Here, it is undisputed that WIS does not have a medical license and is prohibited from rendering the professional medical services that Overlake provides. Moreover, WIS has no primary or secondary liability for Overlake's professional fees; it only collects payments from the patients, or the patients' insurance company, and passes them through to Overlake. If the patients or insurance company do not pay, WIS has no obligation to pay Overlake. Thus, under *Walthew* and *Medical Consultants*, the funds WIS ultimately pays to Overlake for Overlake's professional medical services are not a cost to WIS for the services that WIS renders; instead, these funds are used to pay for professional medical services rendered by a third party, which WIS merely collects and passes through to that third party.

RULE 111

We agree with DOR's initial contention that "unless an exemption . . . applies, a taxpayer owes B&O tax on all income received for the rendition of services." Br. of Resp't at 9. But DOR goes on to argue that "[b]ecause there is no statutory exemption for 'pass-through' payments, and because [DOR] has no statutory authority to create tax exemptions on its own, Rule 111 should be interpreted so that it 'excludes' from tax *only* those amounts that do not meet the statutory definition of 'gross income of the business.'" Br. of Resp't at 11. DOR's argument is circular and unpersuasive. Furthermore, we reject DOR's interpretation of Rule 111, as it renders the exemption meaningless.³ Despite DOR's argument to the contrary, gross receipts do

³ Moreover, DOR insists that Rule 111 is only applicable when the taxpayer is the agent of the payor (i.e., WIS' patients or the patients' insurance companies); but situations in which the taxpayer is the agent of the payee (i.e., Overlake) may also constitute pass-through payments. In such a situation, WIS functions as a collection agency. DOR conceded at oral argument that funds received by a collection agency and distributed to the creditor are not subject to B&O tax. Wash. State Court of Appeals oral argument, *Washington Imaging*, No. 38247-4-II, at 22 min. 34 sec.

not equal gross income; in order for funds to constitute gross income, they must be payments for services rendered. RCW 82.04.080. Here, the funds that WIS takes in and forwards to Overlake are not compensation for services WIS rendered; instead, they are funds WIS passes through to Overlake as would a collection agent.⁴ And if the funds are not gross income,⁵ then B&O taxes are not due and the exemptions need not be applied.

⁴ Because we have determined that the funds that WIS forwards to Overlake do not constitute gross income, we need not address whether these payments constitute pass-through payments under Rule 111. But if we were to reach this issue, *Medical Consultants* would be persuasive and we would reach the same result. In *Medical Consultants*, we addressed Rule 111 and held:

Here, the first prong of the *Christensen* test is not in dispute. The second prong of the test is supported by the undisputed fact that MCN does not have a medical license and therefore *cannot* perform the medical examinations. The monies MCN collects for medical exams are not for MCN's "rendition of services," but rather are passed through to the actual renderers of the medical examination services, i.e., the physicians. Finally, the third prong of the *Christensen* test is satisfied because MCN is not obligated to pay an independent physician unless MCN is first paid by its client. If MCN is paid by its client, MCN's obligation to the physician is solely as an agent of its client. Accordingly, the trial court properly concluded that payments MCN receives for the purposes of paying independent physician bills are not subject to Washington's business and occupation tax.

Med. Consultants, 89 Wn. App. at 48.

Nor is DOR's reliance on *Pilcher v. State*, 112 Wn. App. 428, 49 P.3d 947 (2002), *review denied*, 149 Wn.2d 1004 (2003), persuasive. In *Pilcher*, a hospital contracted with a single physician, Dr. Pilcher, to serve as the medical director and to provide physician services for the hospital's emergency room.

The [h]ospital's only legal obligation was to Dr. Pilcher. The [h]ospital had no separate contract with the physicians Dr. Pilcher retained. Dr. Pilcher had no authority to enter into contracts on the [h]ospital's behalf. Dr. Pilcher was solely liable for paying the physicians. In effect, the [h]ospital was purchasing physician services and management from Dr. Pilcher.

Pilcher, 112 Wn. App. at 439.

Unlike Dr. Pilcher, WIS has no obligation to pay Overlake physicians for their professional services. It merely submits Overlake bills with its own. WIS merely sends patients one bill containing WIS' and Overlake's costs.

⁵ Again, under Rule 111, a business can exclude from its taxable gross income amounts it receives solely as an agent for a client, which the business (as agent) must pay on the client's behalf to third parties. WAC 458-20-111.

CONCLUSION

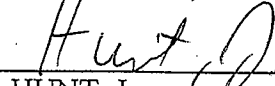
We hold that the money WIS collects and forwards to Overlake for the professional interpretation of WIS' images is not compensation to WIS for "rendition of services," but rather this money is collected by WIS and passed through to those who actually rendered these professional medical interpretation services—Overlake radiologists. Thus, the funds WIS collects for Overlake is not gross income to WIS and WIS need not pay a B&O tax on the portion of the funds that it passes through to Overlake. Accordingly, the trial court erred when it concluded that the payments WIS receives for Overlake's professional services are subject to Washington's B&O tax and granted summary judgment to DOR. We reverse and remand for entry of summary judgment in favor of WIS.

A majority of the panel having determined that this opinion will not be printed in the Washington Appellate Reports, but will be filed for public record pursuant to RCW 2.06.040, it is so ordered.


QUINN-BRINTNALL, J.

We concur:


HOUGHTON, P.J.


HUNT, J.

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

DIVISION II

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ATTORNEY GENERALS OFFICE
REVENUE DIVISION

WASHINGTON IMAGING
SERVICES, LLC,

Appellant,

v.

WASHINGTON STATE
DEPARTMENT OF REVENUE,

Respondent.

No. 38247-4-II

ORDER DENYING MOTION FOR
RECONSIDERATION


RESPONDENT moves for reconsideration of the Court's opinion, filed **September 22, 2009**. Upon consideration, the Court denies the motion. Accordingly, it is


SO ORDERED.

PANEL: Jj. Houghton, Hunt, Quinn-Brintnall

DATED this 2nd day of December, 2009.

FOR THE COURT:


PRESIDING JUDGE

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STATE OF WASHINGTON
BY 

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APPENDIX B

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REVENUE DIVISION

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DIVISION II

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IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

STATE OF WASHINGTON

DIVISION II

BY

DEPUTY

WASHINGTON IMAGING SERVICES,
LLC,

No. 38247-4-II

Appellant,

v.

WASHINGTON STATE DEPARTMENT OF
REVENUE,

ORDER GRANTING MOTION TO
PUBLISH


Respondent.

WHEREAS, the Court believes that the opinion in this case should be published, it is
now

ORDERED, that the final paragraph, reading "A majority of the panel having determined
that this opinion will not be printed in the Washington Appellate Reports, but will be filed for
public record pursuant to RCW 2.06.040, it is so ordered." is deleted. It is further

ORDERED, that the opinion will be published.

DATED this 15TH day of DECEMBER, 2009.



PRESIDING JUDGE

APPENDIX C

WAC 458-20-111

Advances and reimbursements.

The word "advance" as used herein, means money or credits received by a taxpayer from a customer or client with which the taxpayer is to pay costs or fees for the customer or client.

The word "reimbursement" as used herein, means money or credits received from a customer or client to repay the taxpayer for money or credits expended by the taxpayer in payment of costs or fees for the client.

The words "advance" and "reimbursement" apply only when the customer or client alone is liable for the payment of the fees or costs and when the taxpayer making the payment has no personal liability therefor, either primarily or secondarily, other than as agent for the customer or client.

There may be excluded from the measure of tax amounts representing money or credit received by a taxpayer as reimbursement of an advance in accordance with the regular and usual custom of his business or profession.

The foregoing is limited to cases wherein the taxpayer, as an incident to the business, undertakes, on behalf of the customer, guest or client, the payment of money, either upon an obligation owing by the customer, guest or client to a third person, or in procuring a service for the customer, guest or client which the taxpayer does not or cannot render and for which no liability attaches to the taxpayer. It does not apply to cases where the customer, guest or client makes advances to the taxpayer upon services to be rendered by the taxpayer or upon goods to be purchased by the taxpayer in carrying on the business in which the taxpayer engages.

For example, where a taxpayer engaging in the business of selling automobiles at retail collects from a customer, in addition to the purchase price, an amount sufficient to pay the fees for automobile license, tax and registration of title, the amount so collected is not properly a part of the gross sales of the taxpayer but is merely an advance and should be excluded from gross proceeds of sales. Likewise, where an attorney pays filing fees or court costs in any litigation, such fees and costs are paid as agent for the client and should be excluded from the gross income of the attorney.

On the other hand, no charge which represents an advance payment on the purchase price of an article or a cost of doing or obtaining business, even though such charge is made as a separate item, will be construed as an advance or reimbursement. Money so received constitutes a part of gross sales or gross income of the business, as the case may be. For example, no exclusion is allowed with respect to amounts received by (1) a doctor for furnishing medicine or drugs as a part of his treatment; (2) a dentist for furnishing gold, silver or other property in conjunction with his services; (3) a garage for furnishing parts in connection with repairs; (4) a manufacturer or contractor for materials purchased in his own name or in the name of his customer if the manufacturer or contractor is obligated to the vendor for the payment of the purchase price, regardless of whether the customer may also be so obligated; (5) any person engaging in a service business or in the business of installing or repairing tangible personal property for charges made separately for transportation or traveling expense.

Revised May 1, 1947.

[Order ET 70-3, § 458-20-111 (Rule 111), filed 5/29/70, effective 7/1/70.]

NO. 38247-4-II

**COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON**

WASHINGTON IMAGING
SERVICES, LLC,

Appellant,

v.

WASHINGTON STATE
DEPARTMENT OF REVENUE,

Respondent.

DECLARATION OF
MAILING

Candy Zilinskas, states and declares as follows:

I am a citizen of the United States of America and over 18 years of age and I am competent to testify to the matters set forth herein. On January 14, 2010, I provided a true and correct copy of Petition for Review and this Declaration of Mailing to be sent electronically via email to greg.montgomery@millernash.com and monica.langfeldt@millernash.com and by U.S. Mail, postage prepaid via Consolidated Mail Service, to:

Greg Montgomery
Monica Langfeldt
MILLER NASH LLP
4400 Two Union Square
601 Union Street
Seattle, WA 98101-2352

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I certify under penalty of perjury under the laws of the State of
Washington that the foregoing is true and correct.

Executed this 14th day of January, 2010, in Tumwater, Washington.



CANDY ZILINSKAS
Legal Assistant